No. 89-818

IN THE SUPREME COURT
OF THE UNITED STATES

October Term, 1989

MORTON H. JAFFE,

Petitioner,

v

MICHIGAN DEPARTMENT OF TREASURY,

Respondent.

ON WRIT OF CERTIORARI
TO THE MICHIGAN COURT OF APPEALS

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether this Court should defer to the decision of the Michigan Court of Appeals, which found that the Petitioner's disparate business activities do not constitute a "unitary business" consistent with applicable decisions of this Court?

TABLE OF CONTENTS

TABLE OF AUTHORITIES

OPINIONS BELOW

The Opinion of the Court of Appeals is reported at 172 Mich App 116; 431 NW2d 416 (1988) and is reproduced in Petitioner's Appendix A, pp 1A-4A. The Opinion and Judgment of the Michigan Tax Tribunal is unreported and reproduced in Petitioner's Appendix B, pp 5A-14A.

JURISDICTION

The Court of Appeals of the State of Michigan issued its Opinion and Judgment on July 26, 1988. The Opinion is, as indicated above, reprinted in Petitioner's Appendix A, pp 1A-4A. On September 13, 1988, the Petitioner filed a timely Application for Leave to Appeal with the Supreme Court for the State of Michigan. The Supreme Court entered an Order denying the Application on June 7,

1989. The Order is reprinted in Petitioner's Appendix C, p 15A. The Supreme Court entered an Order denying Petitioner's timely Motion for Reconsideration on August 29, 1989. That Order is reprinted in Petitioner's Appendix D, p 16A.

The Petitioner asserts that the jurisdiction of this Court to review the Opinion and Judgment of the Court of Appeals of the State of Michigan is, and can be invoked under 28 USC § 1257(a).

STATUTES INVOLVED

Provisions of the Michigan Income Tax Act of 1967, MCL 206.1, et seq; MSA 7.556(101), et seq, are to the extent they may be relevant, reprinted in Petitioner's Appendix E, p 17A.

STATEMENT OF CASE

Petitioner presents the issue as

> "the proper test to be applied by a court in determining whether a business conducted by an individual proprietor is unitary for tax purposes." Petition, p 2.

Respondent asserts that the Michigan Court of Appeals and the Michigan Tax Tribunal applied the appropriate tests as enunciated by this Court and, based upon the attendant facts, reached a proper conclusion, a conclusion to which this

Court should defer, i.e., that the individual proprietor here involved was not engaged in a unitary business.

Petitioner, Morton Jaffe, asserts that activity engaged in by him in tax years 1981, 1982, and 1983, which was the feeding of livestock and production of beef cattle in Texas, was part of a unitary business activity carried on in the State of Michigan.

Mr. Jaffe's major business activity in Michigan may be characterized as "advertising".

In 1981, 1982, and 1983, Petitioner claimed substantial losses attributable to the cattle raising activity.

In filing his federal income tax returns for 1981, 1982, and 1983, the

taxpayer utilized Schedule F (Farm Income and Expenses) to report losses associated with the cattle operation.

The goods and services associated with such losses were all obtained from non-Michigan sources. Feed, salt, hay, trucking, insurance and veterinary services were all obtained in Texas. The cattle were purchased from, sold to, and delivered to non-Michigan individuals or entities.

No similar goods, services or supplies were obtained by the taxpayer with respect to the advertising business he carries on in Michigan.

For the same tax years, the taxpayer utilized Schedule C (Profit or Loss from Business or Profession) to declare

profits from his advertising business activity.

It has not been demonstrated that any of the items declared on Schedule C are associated with the Texas beef raising activity. The taxpayer himself testified that none of the items of income or expense were associated with the cattle operation.

In reporting his gross income, and more importantly, in calculating his adjusted gross income for federal tax purposes, the taxpayer subtracted his Schedule F losses from gross income and reported his adjusted gross income. Identical sums were reported on the taxpayer's MI-1040's for 1981, 1982, and 1983.

The taxpayer made no adjustments to his Michigan returns for losses associated with the Texas feedlot operation, i.e., in determining his Michigan "taxable income," he did not add back what the Department asserts were out-of-state losses.

Rejecting the taxpayer's assertions of a "unitary business" and finding that the losses associated with cattle operation were "out-of-state losses", the Department adjusted the taxpayer's returns and assessed deficiencies.

A Notice of Intent to Assess was issued; and, following an informal conference, a Final Decision and Order of Determination was issued on April 17, 1985, accompanied by Final Assessment No. C376900, assessing the tax deficiencies with interest.

The taxpayer thereafter initiated the subject action by filing his petition with the Michigan Tax Tribunal on May 15, 1985.

After a trial on the merits, that Tribunal on May 18, 1987, rendered its Opinion and Judgment in favor of the State of Michigan, Department of Treasury.

Petitioner thereafter prosecuted his appeal to the Court of Appeals. That Court sustained the decision of the Michigan Tax Tribunal.

To further understand the nature of Mr. Jaffe's cattle business and the lack of any real, functional, or material interdependence between it and any other business engaged in by Mr. Jaffe, a more

extended reprise of the facts is necessary.

Mr. Jaffe's purpose in indulging in the activity of purchasing, feeding, caring for and selling beef cattle is to make a profit.

Mr. Jaffe does not consider himself an investor.

Mr. Jaffe, alone, makes decisions relative to:

(a) Obtention of financing;

(b) Purchase of cattle;

(c) Purchase of feed; and

(d) Sale of cattle.

He employs no servants or agents in carrying out this business activity.

Mr. Jaffe has cattle purchased in his name by auction buyers. Demonstrating his own business acumen:

(a) Mr. Jaffe determines purchases of cattle based on:

1. Weight;
2. Price per hundred weight;
3. Location;
4. Distance from feedlots;
5. Feedlot performance;
6. Breakeven point; and
7. Market analysis.

(b) Mr. Jaffe makes feed purchases based on:

1. Price;
2. Proximity to chosen feedlot;
3. Whether trucking facilities are available; and
4. Type of grain.

(c) Mr. Jaffe makes decisions to sell based on:

1. Weight of cattle; and
2. Bid price and economics.

The cattle are kept at feedlots in Texas. The feedlot owners are independent contractors who:

(a) Provide the services of a nutritionist;
(b) Have a veterinarian on call;
(c) Have ability to move cattle; and
(d) Inject cattle with antibiotics and growth steroids.

The operation is, to all intents and purposes, a Texas activity. The testimony of the taxpayer himself showed:

(a) The feed purchased by Mr. Jaffe is inventory in Texas. It is held in elevators in Texas.

(b) The cattle are always located in Texas.

(c) The buyer always takes delivery in Texas.

(d) Veterinary services are obtained in Texas.

(e) Insurance is obtained in Texas.

(f) Feed services are provided in Texas.

(g) Medicine is purchased in Texas.

(h) Salt, hay and trucking services are obtained in Texas.

(i) No similar services or supplies are obtained with respect to the advertising operation in Michigan.

(j) Financing has been obtained in Oklahoma.

Further, substantial losses are associated with the feedlot operation for each year reported.

The feedlot operation does not contribute to the advertising business.

In fact, the taxpayer, by his own testimony, further demonstrated the lack of financial interdependence between his two disparate business ventures. To quote from the transcripts:

Assistant Attorney General:

"Of the years that are, of course, in controversy here are 1981 til 1983, you testified that this activity contributed substantially--contributes--to your advertising activity. I would like to understand how it contributes if you tell me you reported losses for years up through and including 1983?"

Jaffe:

"I'm sorry, I don't believe I stated that it contributes to my advertising business; I believe that I stated that it is a segment of my business. I don't believe that I stated that it contributes to the advertising."
Hearing Transcript p 36.

Assistant Attorney General:

"You said that they are financial interdependent, do I take that to mean that if the cattle operations is solvent or on shaky ground, that would affect your advertising activities?"

Jaffe:

"It would affect my total economic picture, yes, sir. If I suffered any losses, I would have to make up those losses from my advertising activities."

Assistant Attorney General:

"How else is there an interdependency between these two activities?"

Jaffe:

"Well, it's because of my advertising activity generating funds which enable me to secure my line of credit."
Hearing Transcript pp 44-45.

Groves (Judge):

"Now again, did I understand correctly, the relationship between the advertising activity and your cattle feeding activity are confined to financial dependence; you defined as something if something goes bad in one area, the other area will suffer?"

Jaffe:

"That's correct, Your Honor."

Groves:

"The advertising activity does not include advertising your own cattle for sale?"

Jaffe:

"No, it does not."
Hearing Transcript pp 46-47.

With respect to the advertising activities, the taxpayer reported gross receipts and expenses each year to the IRS on Schedule C.

None of the gross receipts reported on the Schedule C were derived from the cattle business.

None of the expenses claimed were associated with the cattle operations.

ARGUMENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

This cause presents no substantial federal question and, accordingly, the Petition for Writ of Certiorari should be denied.

Petitioner, contrary to his protestations, was not engaged in a unitary business enterprise during the tax years at issue. Petitioner was engaged in two disparate business activities, (i) advertising in Michigan; and (ii) cattle raising in Texas.

In addressing claims such as Petitioner's, this Court has announced:

> "[T]his Court will, if reasonably possible, defer to the judgment of state courts in deciding whether a particular set of activities constitutes a 'unitary business'" Container Corp of America v Franchise Tax Bd, 463 US 159, 175; 77 L Ed 2d 545; 103 S Ct 2933, reh den 464 US

909; 78 L Ed 2d 248; 104 S Ct 265 (1983).

And, further:

> "[O]ur task must be to determine whether the state court applied the correct standards to the case; and if it did, whether its judgment was within the realm of permissible judgment." Id., at 176.

An analysis of the decisions of the Michigan Court of Appeals and the trial forum, i.e., the Michigan Tax Tribunal, leads to the inescapable conclusion that both the Court and the Tribunal:

(1) examined the particular activities involved consistent with the standards of this Court in F W Woolworth Co v Taxation & Revenue Dept, 458 US 207; 73 L Ed 2d 819; 102 S Ct 3128 (1982), Mobil Oil Corp v Comm'r of Taxes of Vermont, 445 US 425; 62 L Ed

2d 510; 100 S Ct 1223 (1980), and Container Corp of America, supra; and

(2) in light of such facts and the applicable standards, adjudged that the sum and segments of Petitioner's activities did not constitute a "unitary business".

That judgment was decidedly within the realm of permissible judgment. This Court should defer to the state court's judgment.

The Tribunal, consistent with this Court's decisions and the prior decision of the Michigan Court of Appeals in Holloway Sand & Gravel Co, Inc v Dep't of Treasury, 152 Mich App 823; 393 NW2d 921 (1986) analyzed the attendant facts, vis-a-vis, five factors:

(1) Economic realities;

(2) Functional integration;

(3) Centralized management;

(4) Economics of scale;

(5) Substantial material interdependence.

The Tribunal found (and was affirmed in its findings by the Court of Appeals) that:

(a) With respect to economic realities:

> "In considering the first factor, economic realities of the two businesses, the Court, in Holloway referred to Mobil Oil Corp. v Comm'r of Taxes of Vermont, 445 US 425; 100 S Ct 1223; 63 L E 2d 510 (1980) and stated that the form of business is irrelevant to the unity or diversity of the business enterprise, but rather it is the underlying activity that must be scrutinized. In Holloway, the Court held that the activity of Petitioner's incorporated Michigan sand and gravel operations was wholly distinct and separate from the activity of its Texas speedway.

Although petitioner Jaffe engages in business as sole proprietor, and is not incorporated like Petitioner Holloway, the same principle is applicable since the form of business enterprise is immaterial. Petitioner Jaffe testified that such activities of daily management, services and goods necessary for the production of beef are in no way connected to the advertising business. The underlying activity of an advertising business and of a cattle operation is wholly distinct and separate and Petitioner Jaffe fails to meet this requirement."
Petitioner's Appendix B, pp 10A-11A.

(b) With respect to functional integration:

"Although Petitioner Jaffe conducts all administrative services from his sole business office in Michigan and actively engages in beef production for profit, his two businesses are not functionally integrated. Both the advertising business and cattle production operation act independently as to daily activities. The goods and services required for beef production have no relation to the goods and services required for advertising business. There is no flow of goods from one business to the other, nor is there flow of value. Petitioner Jaffe testified that the Texas cattle operation lends

no support, financial or otherwise, to the Michigan advertising business. Petitioner testified that it is his personal and Michigan advertising business assets that allow him to pursue his Texas cattle operation. The fact that Petitioner may oversee both enterprises does not presumptively preclude the finding of separate and distinct businesses. Holloway, supra, p. 832. Consequently, Petitioner has failed to show functional integration of his two businesses." Id., pp 11A-12A.

(c) As to centralized management:

"[P]etitioner Jaffe has shown evidence of centralized management. Petitioner testified that: 1) all feedlot operators are independent contractors who were hired by Petitioner through his Southfield office; 2) Petitioner made all decisions regarding the purchasing, selling and financing of the cattle operation; 3) Petitioner made decisions regarding the purchase of grain except that the feedlot operations determined the mix of ration for the cattle and enlisted the services of a veterinarian; 4) no separate books were kept for each business; 5) Petitioner utilizes the services of one accountant since revenues for both businesses were co-mingled; and 6) Petitioner communicated directly to the feedlot operators. Petitioner has met this requirement." Id., p 12A.

(d) As to economics of scale:

"Here, too, Petitioner Jaffe failed to show evidence that a benefit is obtained through the consolidation of the businesses.

"Petitioner Jaffe purchased his goods and services for the cattle operation in Texas and they were used exclusively for the cattle operation. Although Petitioner conducted all business through his Southfield office, he failed to show how this increased his profits by means of bulk purchases or improved allocation of resources. Also, Petitioner testified that he was able to obtain financing for the cattle operation due to his personal and advertising business assets but failed to show an increased ability to secure financing at a more advantageous rate." (emphasis in original)
Id., pp 12A-13A.

(e) As to substantial material interdependence, the Tribunal, accordingly, concluded:

"In light of the forementioned factors, Petitioner Jaffe has failed to meet four of the five requirements necessary to establish the minimum contacts or nexus required to establish a unitary business.

> Although Petitioner established the factor of centralized management, the totality of the circumstances precludes Petitioner from prevailing on its claim." Id., pp 13A-14A.

The Court of Appeals correctly affirmed that decision.

Nothing in Container Corp, supra, nor in Exxon Corp v Wisconsin Dep't of Revenue, 447 US 207; 65 L Ed 2d 66; 100 S Ct 2109 (1980), suggest a contrary result. Neither case, Respondent submits to this Court, established a singular test for ascertaining whether an activity is unitary. In particular, it did not establish central management as the litmus test. To quote from this Court's opinion in Container Corp of America, supra, 463 US at 179-180:

> "We need not decide whether any one of these factors would be sufficient as a constitutional matter to prove the existence of a unitary business.

> Taken in combination, at least, they clearly demonstrate that the state court reached a conclusion 'within the realm of permissible judgment.'"

CONCLUSION

This Court should defer to the decision of the Michigan Court of Appeals and to the trial forum, the Michigan Tax Tribunal. Each forum correctly applied standards enunciated by this Court to the attendant facts and rendered a judgment within the realm of permissible judgments finding that the taxpayer's activities did not constitute a unitary business.

Taken as a whole, Petitioner's activities were decidedly disparate and attributable in the instance of his cattle raising activities solely to jurisdictions without the State of Michigan. Given the facts, the State of

Michigan could not tax income should he realize income from his business operations in Texas. For like reason, there is no basis for the State of Michigan to allow the taxpayer to attribute his losses from his Texas experience to the State of Michigan in calculating his Michigan income tax liability.

For reasons stated above we would, therefore, request that the Petition for Writ of Certiorari be denied.

Respectfully submitted,

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